I would like first to express my deep gratitude to the East West Center for giving me a 3 month fellowship to do my research. The Washington DC office staff has been wonderful to work with and an inspiration to me. They are doing great work here, and I hope that this office and EWC Honolulu continues to receive crucial funding so their excellent work in bringing Asia in all its many aspects to the attention of policymakers and researchers continues. I also want to thank the EWC, the Japanese Ministry of Economy, Trade and Industry, and the Japan Association for Trade with Russia & NIS for supporting my June research trip to Ulaanbaatar, Beijing, Shanghai and Tokyo. Special thanks is owed to Ms. Kitty Hamilton, an Australian journalist and researcher on Mongolia, who arranged my meetings at Beijing University and the Natural Resources Defense Council in Beijing, and to Nick Miller, a brilliant summer intern at the Korean Economic Institute who supplied me with much material on the Koreas. I could not have completed my research in Mongolia without the total cooperation of many talented researchers and officials from Mongolia’s National Defense University, National Intelligence University, Mineral Authority, Ministry of Foreign Affairs and Trade, Ministry of Defense, the U.S. Ambassador to Mongolia Jonathan Addleton, the Japanese Ambassador to Mongolia Takenori Shimizu, and French embassy in Mongolia, as well as my good friends at the Mongolian Embassy in Washington DC who facilitated many of my meetings. Finally, I especially want to thank the dedicated staff at the Library of Congress Asia Division and Map Office, particularly Ms. Susan Meinheit, who provided me with so much assistance in retrieving books that opened my eyes to the inter-relationships in Northeast Asia which are part of the complex atmosphere that Mongolia must function within. As a Mongolist who also knows China well and Japan somewhat, I can appreciate the great value of taking a specific subject such as Mongolia and looking at it from a multi-faceted regional perspective. Researching Russian and Korean energy policies enabled me to explore Mongolian developments that I already knew well in a much deeper way—which I hope leads to better analysis and forecasting. This research project on the potential impact of new mineral development in Mongolia on North Asian economics and politics has only opened the window on this topic for me.

In the spirit of Geopolitics—defining the circumstances under which a nation will always act to protect its national interests—let me begin by telling you a few interesting comments expressed to me in interviews on my June research trip. These diverse opinions have challenged my analytical skills in understanding what Mongolian and NEA policymakers are facing when we discuss mineral development:
• 2 different high-placed Japanese officials in different meetings asked me: “Are Mongolians Asian people?” Another Japanese official who has led several mineral-related negotiating teams to Ulaanbaatar said that the more he is in contact with Mongolians the less he understands them and their goals.

• A well respected Chinese mineral expert advising the State Council and state-enterprises investing in Mongolia looked me straight in the eye and told me the Chinese are not interested in Mongolian minerals but invest in Mongolia only for political reasons, because they are concerned about “terrorists” from Inner Mongolia receiving assistance from independent Mongolia. When I asked another Chinese mineral expert why the first one denied the Chinese needed Mongolian minerals, he said that the first man had lied to me, and, of course, the Chinese economy needed Mongolian coal and copper for its factories.

• A Mongolian high ranking intelligence official told me that Mongolians know that when they sign a mineral contract with a Chinese state-owned company, the Mongols do not have to follow the terms. However, if Mongols sign a contract with Russians, they must fulfill the terms of the contract or are punished.

• A Mongolian official responsible for executing Mongolia’s mining laws regarding foreign and domestic investment in minerals said that Mongolia has been growing too fast, and if the investment laws are changed to the point of discouraging foreign investors, well, that is not a bad thing.

Introduction

Mongolia traditionally has played a linchpin role in Russia, China and Japan’s strategic views about Northeast Asia, even before Mongolia’s rich mineral resources were proven. In today’s 21st century world of new economic and political realities since the break-up of the Soviet Union and the rise of China, Mongolia has become even more prominent in their self-interested calculations. Now the need for key minerals to feed the Chinese economic juggernaut, as well as the advanced economies of Japan and South Korea, has attracted the attention of the global political and financial investment communities. Mongolia, home to vast resources of coal, copper, rare earth minerals, uranium, gold and silver, had a 17% growth rate in 2011 and in the first half of 2012. Some have called it the ‘Asian Wolf.’ It has the potential to strongly influence
the political, economic, and environmental atmosphere of its North Asian region. Mongolia’s version of resource nationalism is not only of concern to the regional players, but also to the United States’ strategic and political interests in Asia for the next several decades. Nevertheless, there has been insufficient analysis by researchers on the potential impact of the boom in Mongolian mineral development on the eco-political and strategic policymaking of these states, not to mention on Mongolia’s own views about its role in balancing its two giant neighbors with other nations in the Asian region including the United States.

Mongolian mineral resources—statistics from 01.01.2012, Mongolia’s Mineral Authority

- Coal     18,473.2 mil.ton
- Copper    83.807 mil.tn
- Zinc      26.3 mil.tn
- Iron      1,046.6 mil.tn
- Silver    231.87 thou. tn
- Molybdenum 963 thou.tn
- Rare-earth elements 1,459.01 thou.tn
- Tungsten 287.35 thou.tn
- Pewter (tin) 55.8 thou.tn
- Cadmium   6.2 thou.tn
- Arsenic   25.13 thou.tn
- Antimony  74.52 thou.tn
- Uranium   90.03 thou.tn
- Bismuth   17.06 thou.tn
- Gold /earthen/ 221.47 tn and Gold /main/ 2180.94 tn
- Rhenium 9.8 tn

China for more than a decade has been both Mongolia’s largest trading partner and largest foreign investor with 51% of investment in 2011; Canada is 2nd with 8%. Today the US is ranked 9th with 2.39%, while 15 years ago we were No. 1. In 1992 the U.S. imported $6.9 million in goods and exported only $2.3 million. By 2004 the US was importing $239.1 million. But today the US imports only $4.7 million dollars of goods and exports $457.7 million.¹ 89% of Mongolian exports in 2012 went to China.² The amount of coal mining in Mongolia has increased
23% in 2011. China imports only 8% of its coal from overseas, but 43% of that now comes from Mongolia. Over 5,000 Chinese firms operate in Mongolia, with a combined investment of around $2.5 billion.\(^3\) Approximately 65.3% of Chinese FDI in Mongolia is in the “geological prospecting” oil exploration and mining sector.\(^4\) Russia, on the other hand, which had subsidized 1/3 of Mongolia’s budget in the communist era and together with other Cocom countries supplied 95% of Mongolia’s trade in the 1980s, imports only about 2% of Mongolia’s exports in 2011. However, Russia’s influence over Mongolia today comes from the fact that Mongolia purchases 95% of its diesel and petroleum products and about 90% of its electrical power from Russia. A final point is that although Mongolia is undergoing a runaway economic boom, the Bank of Mongolia\(^5\) reports a persistent and growing trade deficit with imports exceeding exports.

In 2012 private companies, domestic and foreign-invested, hold some 3500 mining licenses. 4000 licenses were cancelled without compensation since 2010 for supposed environmental violations. The Mongolian Mineral Authority has indicated it will cancel another 1400 in the next 2 years, and stop the granting of new private licenses for the next 5 years. During this same time period, mineral exploitation will proceed only in the 15 strategic deposits designated by Parliament in its 2006 Mining Law. These deposits are required to be at least 50% state-owned, except for Oyu Tolgoi (OT) copper-gold project which was licensed back in 2003 for development as part of a deal to resolve Mongolia’s outstanding debt to the Soviet Union. OT was originally conceived as a 100% owned Canadian investment and later renegotiated to give the Mongolian Government 34% control. Rio Tinto Corporation in 2009 bought into the project and early this year took majority control of the 66%. The Canadian company, Turquoise Hill,\(^6\) remains as a minority partner. OT is moving forward, having brought over US $2 billion into the Mongolian economy through technology, jobs, and other revenues in 2011. With estimated development costs in excess of US$7 billion and a 40-year plus mine-life, OT is conservatively expected to double Mongolia’s annual GDP by the time it reaches full production around 2017. Initial production of copper concentrate is on schedule to commence in early 2013.

For several decades Mongolia’s largest money earner has been the Russo-Mongol copper joint venture at Erdenet, which is the 4\(^{th}\) largest copper mine in the world. As Mongolia’s largest company, in 2011 it accounted for 13% of the country’s GDP.
**Russian Bear’s “Game Plan”**

It has been said that nobody in Russia understands the global energy security issues better than Putin. Putin’s concept of Russia as “energy super power” is to exploit energy assets for specific political goals. He was quoted as saying: “Russia enjoys vast energy and mineral resources which serve as a basis to develop its economy; as an instrument to implement domestic and foreign policy. The role of the country in international energy markets determines, in many ways, its geopolitical influence.”

Anita Orban sees the primary motive of Russia’s energy imperialism is to increase its power and the most effective means is expanding its political-economic presence in energy sphere. “These aims are conditioned by the Russian leaders’ perceptions of the country’s role in the balance of power and the resources available to the Russian state.” Putin’s policies have three overarching themes—restoring military security, using energy development to obtain security, and rebuilding Russia greatness. After a 2004 spike in oil prices, although Russian net amount of energy exported did not increase in any large quantity, the value of exports increased so it could be used as an “energy weapon.” Russian energy policy is a key issue in global energy policy and it is crucial for Russia. The price of oil in 1998 was US$10-15 per barrel. In 2008 it was $140 per barrel. Prices have slumped with 2008 crisis so it is in $75-100 range. This price increase is what revived the Russian economy.

One-half of Russian crude oil is exported. When the Russians saw the stagnation of their major market, Europe, during the recession, they decided to move more vigorously into the East Asian market, because, for example, in 2009 China, Japan, and SK accounted for almost 17% of world oil consumption and 21.6% of imports. Thus, we can see “impressive eastward shift in oil and gas development in Russia” in a quite successful campaign to partner with China to develop energy trade. The Eastern Siberia Pacific Ocean (ESPO) pipeline project Rosneft became exclusive supplier of crude to China in 2009. When Putin called ESPO a ‘geopolitical’ project, he was saying that for Russia geopolitical goals outweigh business consideration.

Putin has renationalized Russia’s energy resources industry and eliminated many inefficient mines and fields. This required expanding the state’s role in the economy through powerful corporations, termed national champions, to compete in the world market. These state companies get preferential treatment from the government. Because of a revised tax regime, imports of oil, gas, and even coal from Central Asia and Caspian countries has become cheaper.
than developing new Russian fields in Siberia and the Far East. According to Russia’s Energy Strategy (Govt. of Russia Federation, 2009), eastward export share of crude and petroleum products was 8% in 2008, but expected to reach 22-25% in 2030. Gas exports to Asia were expected to grow from almost 0% in 2008 to 19-20% in 2030.

Russian Strategy to 2020 projected increasing coal use in the heat and power sector to lower domestic dependence on gas, so that the gas could be exported at greater profit, moving 20% of power from coal in 2000 to 21-23% in 2020. This would mean that coal production would have to rise almost 75% by 2020. However, there are problems about achieving this goal: 1) the coal sector does not attract sufficient investment; 2) its competitiveness with natural gas; and 3) environment implications. At the same time after 1999, Russian coal exports to Asia have surged, and prices have increased after 2000. Additional future coal export increases depend on development of port capacity in the Pacific.

Russia has leveraged its abundant energy resources and energy wealth to restore the Russian economy, consolidate power domestically, and then project it abroad. Putin’s plan to use oil and gas exports as a cartel to rebuild Russia was aided by the steep rise in hydrocarbon prices in the last decade. Published energy strategy pronouncements under Putin have emphasized that energy security is the most important element in Russia’s national security. An important element of this strategy was creation in April 2002 of a list of strategic natural resources, including fossil fuels and mineral deposits above a certain size that was codified into legislation in February 2004. The Russian state became the developer of “strategic” businesses and forced out the private sector. Foreign invested deposits were confiscated for “booking” reserves not developing them. Windfall taxes imposed on energy profits generated billions of dollars supposedly to fund energy investment in developing new deposits, but were mainly distributed for politically popular social benefits and pensions and to build up a Reserve and National Wealth Fund. Russia expects in the next decades that West Siberia will continue to be the major domestic supplier of oil, gas, and coal., even though these West Siberian fields are 65-75% depleted. East Siberia and the Far East will become net exporters of these same energy products, although less than one-tenth of Eastern Siberia actually has been explored for fossil fuels.

Putin in the middle of the 2000s also felt it necessary to re-engage with Mongolia, which had become by then overwhelmed by Chinese investment. Since then, he has reinvigorated ties
with the former satellite through high-level state visits and more economic and military aid. But at the same time, Putin has strong-armed the Mongolians by cutting off already paid for diesel and oil supplies at different times. The most famous example was in May 2011 when he interjected Russia in a non-transparent fashion into the short-list for foreign investors for Tavan Tolgoi (TT) coal mine by forcing the Mongols to include the Russian state-owned Russian Railway which had not even made a bid. He wants to be involved in TT not just from a strategic point of view—not ceding the field to the Americans and Chinese, but also because it is clear that with coal production faltering but coal demand growing inside of Russia, developing Mongolian coal resources is a cheaper alternative to finding and extracting coal from inhospitable East Siberian deposits. Putin particularly desires Mongolian uranium resources in order to strengthen his control over the uranium market price.

Mongolian policymakers have noted that despite Putin’s success is restoring Russia’s economy and projecting outward Russian power through his energy security policies, his actions have not resolved the population crisis Russia faces in its eastern provinces. While the Russian population in 2000-2010 saw a total population decrease of 3.4%, in the Far East the decrease was 6.8% because of unemployment and quality of life issues. Of more concern is the accompanying trend of Chinese traders and illegals pouring into Siberia and the Far East in numbers which threaten Russian control of major cities such as Vladivostok. If this migration is not rectified, it is easy to imagine loss of great amount of Russian territory in the east to China or independence movements. Such a result for Mongolia is particularly dangerous to its national sovereignty.

**Chinese Dragon’s “Great Game”: The Outgoing Strategic Policy**

A Chinese energy specialist has stated that “The fundamental aim of China’s energy strategy is to support and guarantee the successful attainment of its social and economic development goals.”²² Among these goals are: 1) provide support for an average growth rate of 7.5% and meet people’s energy consumption demands; 2) bring production and consumption of energy in line with population changes, resources and environment; 3) enhance security in the energy supply. China’s key concerns regarding energy and energy minerals are to increase the overall capacity of energy supply, especially oil, and reduce insecure elements; increase clean energy supply; reduce pressure on resources and the environment; improve energy efficiency,
conservation and reduce consumption; diversify the energy supply while reducing the risks to ensure energy supply security; strengthen the role of the market in allocation of resources while always maintaining the government’s strategic leading role as well as its policies in guiding energy development and conservation; and reduce price distortions.23

By 2005 China accounted for 13.6% of total world energy production. Although the 2nd largest energy-producing country in the world next to the US, it also is the 2nd largest consumer of energy resources mostly in coal, because China’s energy power policy is based on coal production and usage. In 2005 oil and natural gas only supplied 24% of its power while hydro and nuclear power represented 7.3%. In the 2000s China was importing 10% of its energy products.

The all-important coal industry in China intersects politics and economics. It was a pillar of China’s planned economy and industrialization under Mao. In the 21st century the country still has not switched its energy to oil like other modern economics. Whole regions of China have their growth tied to coal mines and the accompanying environmental damage and deaths have led to social unrest. Total verified basic reserves of coal are estimated at 114 billion tons.24 After 2002 China’s position in the international coal market changed dramatically. It experienced domestic energy shortages so it reduced its coal exports. However, in 2006-2007 the Government changed the tax structure to encourage coal imports and abolished the tax incentive for exports and the import duty. Even though China in 2009 produced 2971 million tons of coal,25 that same year it registered an import balance of over 100 million tons. In recent years much of it came from Australia, but in 2011 China’s major coal partner became Mongolia.

One of the keys to understanding Chinese energy strategy is to recognize that, although China has the 3rd largest reserves of coal resources after Russia and the US, these are not well placed. The geographical separation of coal production and consumption is a major problem. Shanxi and Inner Mongolia account for ½ of the reserves and over 40% of production, but the industrial consuming regions on the southeastern coast are the main consumers.26 Moving the coal from producing sites in the north ties up the rails. Another significant factor is that the quality of most of China’s coal is poor. It is short of coking coal, which must be imported.

Furthermore, because of the explosive growth in the economy, China’s coal reserves only will last a few more decades into the future. Nevertheless, its medium and long-range sustainable development strategy for the energy sector includes relying mainly on domestic coal supplies
and maintaining coal as the energy foundation; accelerating large coal field production; diversifying development of new resources including more nuclear power; and increasing the import of oil and gas from outside China. Today China’s coal industry is the world’s largest, and it is importing a small, but growing, amount. Coal accounts for 70% of China’s primary energy production and consumption. 70% of its energy consumption still is supplied by coal and 50% of its domestic coal is used for electricity generation.

Does China have an energy security policy? Several years ago, this question did not have a clear answer. According to Roger Robinson, Jr., Chairman of the U.S.-China Economic and Security Review Commission, and C. Richard D’Amato, Vice Chairman, the answer is YES: “China has a comprehensive energy security strategy, consisting of demand reduction, diversification, leveraging bilateral relationships with key Middle East suppliers, building stronger ties with Russia, and establishing a market position in Central Asia.” Kang Wu, head of the China Energy Project at the East West Center, has concluded that because of the rise of oil imports and price volatility in global oil markets, energy security is a big issue in China. This was evidenced in China’s 2001-2005 10th 5-Year Plan. It mentioned energy security and ensuring energy supply security for the first time as a precondition for implementing China’s overall energy strategy. Among the policy goals were diversifying sources of energy; increasing oil and gas imports from Russia and Central Asia; increasing overseas investments by state oil companies; broadening ways of trade to avoid risks; increasing investment in oil and gas infrastructure and opening more import channels; participating in the formation of a regional community; and establishing a regional energy security system. For the future, the Chinese believe that oil is not a likely replacement for coal, but natural gas is a better possibility.

Dean P. Girdis, Director of PFC Energy (a global energy strategy firm), believes there is NO Chinese comprehensive energy security strategy, only a leveraging of bilateral relations using political clout and market advantage by supplying money and weapons, and a desire to build stronger energy ties with Russia. He sees Chinese state-owned companies (SOCs) aka national-owned companies (NOCs) as vehicles to improve China’s overall energy security by promoting investment in overseas gas and oil. Such support is created by high level political delegations and capital infusions. However, he does not see any clear SOC investment strategy because they “are increasingly pursuing strictly commercial investment strategies that may not fully take into consideration broader objectives of energy security for China.”
It would appear the question finally was answered when in January 2010 the National Energy Commission (NEC), headed by Premier Wen Jiabao with Vice-Premier Li Keqiang as deputy, was established to take charge of the country’s energy policies for better coordination in formulating strategy and planning development to maintain CCP legitimacy as China concentrates on energy supplies and relies more heavily on imports. The commission is responsible for drafting national energy development plans, reviewing energy security and coordinating international cooperation. Part of the overall strategy has been to deliberately nurture closer relations with Russia, and use the Shanghai Cooperation Organization to build trust so that Russia sees China as a preferred economic partner over Japan.

China has seen Russia as a strategic partner since the mid-1990s. In principle, it seems there is a good match for future energy cooperation between Russian natural resources and the Chinese market. Development of Sino-Russian energy ties is the most important factor driving “strategic convergence” of China and Russia. Russian supplies can be brought overland through Central Asia and Mongolia, so this has strategic significance for China. However, there are significant points of tension, including slow Russian development of its resource deposits and transport (pipeline) infrastructure; the unpredictability of Russian decision-making and verbal agreements; Sino-Russian traditional rivalry in Central Asia and Mongolia; and attempts by Russia to play off China and Japan. Russia’s deliberately in-action and ambiguous energy and export strategies have led the Chinese to look to other Asian mineral suppliers such as Kazakhstan and Mongolia.

This analyst believes China does have a general energy security model based on the success of its SOC oil companies in the last two decades of globalization. This Out-Going Energy Strategy utilizes SOCs to buy up and exploit diverse mineral deposits overseas and is the system China has employed in Mongolia. Even if one believed China’s mineral’s acquisition policy in Mongolia was based on national security and “anti-terrorist” objectives (as explained by the Beijing University professor I quoted in my opening remarks), there are now strong indications that the Chinese methodology that caused the SOEs to reorganize and concentrate more on business functions, is at a crisis point and is less and less effective in the Mongolian case. This is because the strategy and its execution are in the hands of the economists and SOC business executives, not the foreign policy specialists on Mongolia who comprehend Mongolian mentality, history, and the role of regional geopolitics.
Japanese “Game Plan”

Resource-scarce Japan has few domestic energy resources and is only 16% energy self-sufficient as of 2012. It is the world's largest importer of LNG, second largest importer of coal, and the third largest net importer of oil. Its total import of mineral fuels in 2011 amounted to $274.3bn tons, compared to $198.6bn tons in 2010, an increase of 38.1%. The ratio of Japan's mineral fuel imports to her total imports soared to 32.04% in 2011 from 28.60% in 2010, mainly due to the increases in the volume of import of petroleum products. Meanwhile, Japan's growing need for even more gas, oil and coal to offset lost nuclear power generation after the Fukushima accident in March 2011 pushed imports even higher as the country posted a trade deficit in January-June 2012 of 2.9 trillion yen ($37.4 billion). This was due to a rise in fuel imports for power plants, after the shutdowns of all but two of the country's 50 nuclear reactors. In recent years Japan’s plan for resource mineral acquisition has been one of diversification from heavy reliance on Middle Eastern petrofuels. Nuclear energy was the original preferred solution for decades with natural gas a strong second.

Today with the uncertainty about Japanese nuclear energy policy going forward, Japanese policymakers are looking at immediate alternative power sources even more intensively. Natural gas is increasingly important in Japan’s energy planning and is currently the preferred fuel-of-choice for the shortfall in nuclear capacity. This meshes well with the Japanese desire to increase its Russian hydrocarbon imports. Increased import of natural gas was thus made necessary, even in the backdrop of an escalation in the prices of mineral fuels globally.

Although Japan mainly relies on oil for energy, oil’s share of total energy consumption has declined from about 80% in the 1970s to 42% in 2010. Modern Japanese history has the recurring theme that “securing stable supply of mineral resources is a matter of national importance, namely maintaining and strengthening the industrial competitiveness is, in other words, an imperative issue for Japanese economic security.” In recent decades Japanese national energy strategy is based on the concept of companies seeking high-profile upstream exploration and production projects involving major investments in overseas ventures with government backing. The government’s 2006 Energy Strategy Plan encouraged such projects around the world to secure a stable supply of oil and natural gas. The Japan Bank for International Cooperation offers loans at favorable rates which enables Japanese companies to win bids in key producing countries. “The government's goal is to import 40 percent of the
country’s total crude oil imports from Japanese-owned concessions by 2030, up from the current estimated 19 percent. The overseas oil projects are primarily located in the Middle East and Southeast Asia, and involve major Japanese oil companies such as Inpex, Cosmo Oil, Idemitsu Kosan Co., Japan Energy Development Corporation, Japex, JNOC, Mitsubishi, Mitsui, and Nippon Oil.

Coal remains an important fuel source and accounted for 43% of fossil fuel-fired generation in 2011, according to the International Energy Agency. Domestic coal production came to an end in 2002. Japan imported 207 million short tons in 2010, mainly from Australia. Coal-fired power plants still provide about 25% of Japan's power. With three facilities presently under construction and the potential to increase the output of existing plants, coal-power generation could jump. But several coal-fired plants were damaged in the 2011 earthquake and have yet to resume operations. Because of this, coal was not used as a substitute for nuclear power and actually experienced a negative growth in 2011. An additional factor is that more coal usage would violate Japan's 2010 Basic Energy Plan, which called for reducing coal power from 25% to 10%. However, new clean coal technologies are being considered to meet environmental targets.

The present Japanese power crisis and the growing importance of Russia and its transportation network to solving Japanese energy resources supplies all are impacting on Japanese policymakers approach to Mongolia and its minerals. Although a very generous aid donor to Mongolia in the past 2 decades, Japan saw Mongolian minerals mainly in the context of selling to established Chinese customers, not bringing the minerals back long distances to Japan. Japanese advisers to the Prime Minister told me in June that the Japanese Government still did not understand that Mongolia is important within NEA, or support a trade diversification policy which fully includes Mongolian mineral products. In the past, Japanese investment in Mongolian minerals was supported by METI as a minor part of its diversification and long range mineral acquisition strategy. Sources in METI explained that interest in Mongolia had been high 5 years ago, but because of failure to turn negotiations into working contracts, pursuit of Mongolian mineral joint ventures had fallen off. The Japanese government and businessmen feel they have trouble communicating with Mongols. They negotiate but do not make progress in implementing agreements. The Japanese were very angry when shut out of the short list for TT coal project and are uncomfortable with the Mongolian suggestion to partner with the Russians as a way to
become active in it. Since the Japanese now are cooperating with the Russians on new pipelines for natural gas and building new LNG facilities on the Pacific coast, there is the potential to expand this Russo-Japanese cooperation into Mongolian mineral development, such as participating in Mongolian natural gas and oil extraction. Because of the present anti-nuclear climate in Japan, interest in Mongolian uranium deposits and arranging a nuclear waste storage facility for Japanese waste materials inside Mongolia are on the backburner. However, the Japanese still hold strong interest in rare earth mineral development in Mongolia. Nevertheless, rail and pipeline transportation problems remain major inhibitors to any major increase in mineral investment.

South Korean and North Korean Strategies

A) South Korea

South Korea has limited mineral resources; however, it only possesses 10% of the coal and iron deposits on the Korean peninsula—the rest are located in North Korea. It is already one of the top 10 energy consumers in the world, and the International Energy Agency expects its power needs to increase 37% between 2006 and 2020. The ROK is the world’s fourth largest oil importer and second largest coal and LNG importer after Japan. All energy imports arrive by sea because of the division of the peninsula.

“Because of its high dependence on external sources for energy and mineral resources, Korea’s strategies to secure them are in essence diversification of energy and mineral supply sources and their overseas development.” 41 For energy in particular, Korea seeks to secure a stable, cost-effective, and environmentally-friendly energy supply. The government focuses on natural gas, bituminous coal and nuclear power, while seeking to reduce its reliance on imported oil. Even after the nuclear accident in Japan in 2011, it sees its nuclear power (15%) as an increasingly important part of its energy strategy, but must import all uranium. Korea has invested in numerous overseas resource projects to secure supplies and has set targets to import an increasing portion of imports from Korean-owned foreign operations. It is especially interested in developing Russian oil deposits. However, South Korea’s energy strategy is complicated by the North Korean situation and any conflict or unification scenario would increase energy demand.
South Korea in 2011 was the 3rd largest trading partner of Mongolia and the 4th largest FDI investor with an investment value of over US$255 million since 1990. It was also a key donor, providing $137 million since 1990 in loans and grants. South Korean major investments are in real estate, telecommunications, and banking, but it has moved into the mining sector. The state-owned Korea Resources Corporation, steelmaking company Posco and Korea Electric Power Corp. made an unsuccessful bid for the TT Western Tsankhi coal field. In March 2011 Lotte E&C-led South Korean consortium signed a preliminary deal with Mongolian Railways to build a 1,040-kilometer railway in Mongolia. This will link up to the Russian-gauge main north-south railroad in Mongolia which goes across the border through Siberia, and thus may be the catalyst for South Korea to acquire Mongolian raw minerals such as coal.

B) North Korea

North Korea has substantial mineral deposits, including magnesium, iron, tungsten, anthracite coal, molybdenum, and gold. Most are unexploited, but if developed could compete with Mongolia’s deposits. Mining operations are few due to lack of electricity, materials and equipment, although since 2000, iron ore and coal production has increased slightly. Foreign companies from China, Japan, US, and UK have participated in about 25 mining projects. China is the major trade partner with 58% of total exports in 2009 represented by minerals and mining products. Since 2003, Chinese companies have aggressively been involved in 20 mining projects. North Korea was China’s 2nd ranked anthracite coal supplier in 2009. China holds 75% of the North Korean known foreign joint ventures and is the major supplier of petroleum to North Korea.

The Rajin-Sonbong (aka Rason) region in North Korea has strategic significance as the northern-most year-round ice-free port in NEA. It was identified in the United Nations-backed Tumen River Development Project as a potential geostrategic transit point for the shipment of goods to landlocked Northeastern China, Mongolia, and the Russian Far East. North Korea has tried to involve Russia in a competition with China for access to the port by pursuing deals with both sides simultaneously. The Chinese Chuangli Company contracted to develop Rajin’s port number one, reportedly for a period of only ten years, while Russian investors have been offered
a fifty-year deal to develop the second part of Rajin. Initial plans are to export Chinese coal to Southeast Asia and Japan (Global Times Online, March 10). It is thought that China’s northeastern provinces would greatly profit from the maritime access Rajin-Sombon port facilities would bring to the East Sea/Sea of Japan. South Korea and Russia are planning to build a cross-border railway link between Rajin-Sonbon Port and the Chinese border city of Hunchun, and rebuild a rail line between Rajin and Russia’s Khasan. If international rails are built to North Korean ports, Mongolia will have an answer to its northern transportation route problem and a new access to Asia-Pacific markets.

US embassy cables from as far back as 2004 released by WikiLeaks has followed working and living conditions of DPRK workers sent to Mongolia with the permission of Pyongyang authorities. In 2011 the annual quota was raised to 3000 North Korea laborers with their salaries paid directly to the North Korean Government via the DPRK embassy in Ulaanbaatar. These workers work on construction sites and in textile factories such as the Scottish joint venture Eermel cashmere company, but it is speculated they could move into mining operations.

MONGOLIAN WOLF STRATEGY

In this environment how then should a small nation like Mongolia, wedged between giant China and Russia, see its role today in the world? When I travelled to Mongolia to talk to Mongolian officials and researchers about defining a Mongolian strategy for mineral development, I received many answers: ‘No, there isn’t one,’ from the generals; ‘yes, there is one,’ from the Ministry of Foreign Affairs and Trade and Mineral Authority (citing the 2010 National Security Concept and 2006 Mining Law with its revisions); ‘no, but there should be one,’ from the intelligence community. However, I do believe there is a general mineral development strategy in Mongolia which transcends parties and administrations—even if its details are not yet specifically articulated.

Mongolian policymakers believe that geography is the major, decisive factor in shaping the country’s destiny. Mongolia for centuries was a weak pawn whose fate was determined by the nature of the Sino-Russian relationship. Its decision in the beginning of the 20th century to align with Russia preserved its national sovereignty. When the Soviet Union disintegrated, Mongolia had to define and pursue its own national priorities. Thus, it abandoned reliance on just
one state and one ideology and embraced a multi-pillared foreign policy.\textsuperscript{48} It sought a balanced, but not necessarily equidistant, relationship with its two neighbors, and declared itself a Nuclear Free Zone.\textsuperscript{49} It made integrating into the Asia-Pacific region a priority, and considered its civilization and national identity as undeniably Northeast Asian.\textsuperscript{50} It understands that NEA’s economic growth requires secure energy resources and sees its own mineral deposits, which include oil, natural gas, and uranium, as the motivation for regional players to implement an ’Infrastructure Linkage Strategy’ so Mongolia can build up its poor rail and pipeline freight transportation options to become a transit corridor. Concurrently, Mongols believe that NEA cannot fully proceed with economic cooperation without recognizing the remaining Cold War (Korean peninsula) and historical (Sino-Mongol, Sino-Japanese, and Korean-Japanese) security challenges which push countries to increase bilateral defense relations.\textsuperscript{51} Therefore, Mongolia promotes its growing military relationship with the US and NATO.

It is quite clear that since 2006 Mongolia has emulated many Russian energy security policies and legislative forms, primarily in reaction to massive Chinese investment in its economy. In that year it amended its liberal Mining Law to create a government-owned strategic deposit list based on deposit size with state control of up to 50%--a Putin-devised formula. Mongolian Mineral Authority officials forthrightly state that in the next 2 years this list will be revised and many more deposits will be added. In 2006 the government imposed a 68% windfall tax on gold and copper, which severely delayed sizable foreign investment and finally was repealed.\textsuperscript{52} In the last 3 years Mongolia has cancelled about 4000 private mining licenses for environmental violations and plans to cancel another 1400 for non-development.

In May Parliament passed the \textit{Strategic Entities Foreign Investment Law (SEFIL)}, just before parliamentary elections. These mining law amendments govern foreign investor participation in Mongolia’s mining sector and especially limit the activities of foreign state-owned companies (SOCs). These amendments were in direct response to voter concerns that Mongolia’s sovereignty was being threatened by the acquisition of mineral resource rights in legal stock takeovers from western or Mongolian private firms by Chinese SOCs. The specific catalyst was the attempt by the Aluminum Corporation of China (Chalco) to buy up 58% control of the Canadian company Ivanhoe’s private coal mine called Ovoot Tolgoi situated near the Chinese border. Although all Mongolian foreign and domestic observers were certain that no new mining-related legislation would be enacted prior to the June 28th elections, the April
announcement by Chalco and Ivanhoe of their intention to finalize the deal on July 4th provoked a violent wave of ‘resource nationalism’ sentiments from policymakers and the populace alike. The Ministry of Mining revoked the mining license for Ovoot Tolgoi’s thriving coal operations and the Parliament with approval by the government rushed forward with legislation that thwarted the takeover. The Chalco bid, after several extensions to allow for more negotiations, finally was withdrawn on Sept. 3rd but the new amendments remain in place.

The firestorm provoked by Chalco has not and is not ended. In June the Mongolian Cabinet with approval of the President decided that no new private mining licenses will be distributed for the next 5 years. In September we heard that almost one-third of the Parliament is demanding the re-negotiation of the OT investment contract in the fall 2012 parliamentary session. It appears that the once favorable Mongolian mineral investment environment has been turned upside down for all foreign investors. What is happening in Mongolia? What more will happen?

My conclusions about Mongolia and its mineral development policy are based on the fact that Mongolian policymakers and politicians of all political persuasions want to modify the present foreign investor climate of the past decade because, bottomline, they see it as a failure in many ways, despite all the high economic growth. Opening Mongolia’s economy to the outside world during the past 20 years did not prevent the monopolization of the economy by one of the country’s two neighbors. This time it was by the Chinese, and this simply is not acceptable or sustainable. Mongols blame the western financial experts and multilateral organizations, seeking economic development regardless of how it could hurt the country’s sovereignty and national identity, for institutionalizing policies that promoted Chinese interests at their expense. Mongolian people were encouraged by western economic advisers and their own politicians to think that development meant they would become rich quickly, and now they feel that the monies realized from the foreign investments have been funneled into the hands of foreigner businessmen and their own corrupted officials. This thinking, whether correct or not, has not been countered by sound argumentation. In fact, the constant drumbeat of criticism by westerner observers of “corrupt practices” has increased the cynicism within Mongolian society and tempered its respect for free markets.

As a result, today Mongolian leaders are employing a resource nationalism strategy based primarily on national security objectives, while modifying unregulated democratic, free market
structures. Mongolian policymakers for the past decade have studied the economic development experiences of other countries, especially Russia’s, for successes and failures in resource development. A fundamental difference between the Mongols and Russians is that the Mongols have learned from their long history sandwiched between two giant powers to appear to be everything to all foreign partners while in fact pursing their own agenda.

Their overall development strategy now is to rebalance to some extent Chinese trade monopolization of Mongolian economy by expanding and diversifying the players in the foreign investment pie and to tighten foreign ownership regulations through parliamentary legislation with stronger central and local government oversight. This they will accomplish by retrenching and renationalizing many existing mineral deposits through review of mining deposit licenses which results in outright confiscation. The reasons cited for revocation will be that license holders have caused environmental damage and/or non-development (booking) of sites. These politically correct rationales will be offered to avoid international court cases and payment of compensation, but at the same time result in favoratory or discriminatory decision making that will add volatility to the investment climate. The Mongolian government does understand that such actions over the next five years will result in a cooling off period that will slow the pace of foreign investment and mineral development in general. They are not concerned because the policymakers believe they can develop revenue streams from anticipated continuing, ever higher, energy resource prices, ‘advanced tax payments,’ and promises of future favors to the gullible, mineral-seeking foreign investment community. Such a view of economics is both the result of recent Mongolian democratic experience with a very generous foreign donor regime as well as of successes from their historical manipulation techniques perfected over centuries of dealing with Chinese emperors and Russian czars.

The Mongolian government will place tax and concession revenues from the mining sector into its Human Development Fund, but, emulating the practices of Putin, use the monies to make payouts to the populace at times which can influence domestic elections, instead of based on sound fiscal timing. The Mongols will revise and develop their mineral agreements to demand that foreign investors finance power plants, mineral processing industries to produce value-added products, and domestic rail and road transport infrastructure. They expect the growth of domestic mineral production to fall in the near term; however, they are confident they will receive increased revenue from these fewer higher-value products. Mongolia will ask Japan and the
Koreas to partner with Russia in building pipelines and expanding rail routes north to the Pacific to enable Mongolia to develop access to new trade partners and decrease reliance on the south-to-China transport route. However, Mongolia will not accept the mutual dependence theory for its relationship with Russia. Leery of their energy dependence on Moscow and concerned by Russia’s penchant to cut off hydocarbon and power supplies and manipulation of energy companies as instruments of foreign policy, the Mongolian government actively will reduce its reliance on Russian diesel, oil products and power by sponsoring quick, home-grown alternatives, even if they are less profitable and efficient because of their small-scale. All of these policies, the major pillars of a mineral development strategy, will continue for the rest of this decade, regardless of changes of political parties and administrations. Nevertheless, if political and economic events in the NEA region warrant, Mongolia has the mentality and track record to readjust its overall strategy, if necessary. Although they will make changes in conformance to WTO and existing international legal practices, Mongols, embued with a cultural mindset from their nomadic ancestors, will approach mining and economic development with great flexibility and thus perhaps frustrate their foreign partners.

4 Ibid.
6 The name was changed in 2012 from Ivanhoe.
10 Pami Aalto, Russia’s Energy Policies, 3.
14 Tabata and Xu, 159.
15 Russia Energy Survey, 149.
19 He put 1000 enterprises under state ownership via List of Strategic Enterprises and Strategic Joint Stock Companies. Most were in the defense-industrial complex but the list also includes state-controlled energy companies including Transneft, Transnefteprodukt, Gazprom. The list has been revised several times. Philip Hanson, “The Sustainability of Russia’s energy power,” in Russian Energy Security and Foreign Policy, 6 & 40, nt. 66 (See “On Approving the List of Strategic Enterprises and Strategic Joint Stock Companies,” Vremya Novostey, 6 August 2004).
23 Ibid.
25 Wright, 35. The US was the number 2 producer (919 million tons) and India was ranked third with 526 million tons produced.
26 Ibid., 20.
27 China’s willingness to import hydrocarbons and energy minerals from Russia is seen by Chinese imports: 2.1% of its oil for its energy production in 2000, over 10% in 2005 and 2006, and 7.5% in 2009. Tabata and Xu, 171.
29 Testimony of Kang Wu, China’s Energy Needs and Strategies, 42.
30 Testimony of Dean P. Girdis, ibid., 45-46.
31 Ibid., 50.
35 Elaine Kurtenbach, “Japan Back to Trade Deficit, $6.5 billion in July,” The Big Story, AP, August 22, 2012.
37 Tabata and Xu, 159.
40 Energy Information Administration, June 4, 2012.
44 Ibid., 212.
“North Korea’s ports Mongolia’s gateway,” Bloomberg, June 19, 201.
http://www.nkeconwatch.com/2022/10/14/north-koreans-working-in-mongolia/
Outlined in Mongolia’s “Concept of Foreign Policy” and “National Security Concept of Mongolia” in June 1994 and updated in the “National Security Concept of Mongolia” of July 15, 2010.
Proclaimed by President P. Ochirbat to the 47th session of the United Nations General Assembly on September 25, 1992.
Rescinded January 1, 2011.